

WATER/ICRJ/RHG

Decision _____

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF
CALIFORNIA**

In the Matter of the Application of CALIFORNIA
WATER SERVICE COMPANY U-60-W
requesting for an order from the California Public
Utilities Commission to issue and/or sell on or
before December 31, 2010 not exceeding in
aggregate amount \$250,000,000 of any
combination of (1) shares of its common stock, (2)
shares of its preferred stock, or (3) debt securities
and for exemption from the Commission's
Competitive Bidding Rule.

Application 04-03-033
(Filed March 30, 2004)

**OPINION GRANTING AUTHORITY TO ISSUE DEBT AND EQUITY
SECURITIES**

Summary

This decision grants California Water Service Company (Cal Water) the authority requested in Application (A.) 04-03-033 (Application).

Cal Water requests authority, pursuant to §§ 816 through 830 and 851 of the California Public Utilities (Pub. Util.) Code to issue, sell and deliver not exceeding \$250,000,000 in aggregate principal offering amount of common shares, preferred shares or debt securities (New Securities) and for exemption from the Competitive Bidding Rule in relation to sale of debt securities \$20,000,000 or less in any one issue and to any one purchaser during any calendar year.

Notice of the filing appeared on the Commission's Daily Calendar of April 1, 2004. No protests have been received.

Background

Cal Water is a California public utility corporation engaged principally in the retail water business, providing service in many localities in the State of California extending from Chico in the north to the Palos Verdes Peninsula in the south. Cal Water is one of the five operating subsidiaries of the California Water Service Group (Group).

Cal Water serves 439,900 customers and has 24 systems, subject to regulation by this Commission. Cal Water accounts for 96% of the total customers and 96% of the total operating revenues of Group.

Discussion

Cal Water has previously issued long-term borrowings and equity securities authorized by this Commission. The most recent financing authorizations are as follows:

Decisions (D.) <u>No.</u>	<u>Authority</u>	<u>Type</u>	<u>Remaining Authority</u>
D.96-10-062 ¹	\$115,000,000	Debt/Equity	none
D.02-03-017 ²	\$250,000,000	Debt/Equity	none

The decisions also approved some exemptions from the Competitive Bidding Rule.

Cal Water now seeks authorization to obtain New Securities in an aggregate principal amount not to exceed \$250,000,000 through the issuance and sale of common stock, shares of its preferred stock, and debt

¹ Cal Water paid the full fee of \$63,500 for this financing order, as required by Pub. Util. Code § 1904(b).

² Cal Water paid the full fee of \$131,000 for this financing order. At that time, none of the proceeds of the proposed issue were earmarked for refunding or retirement of debt for which a fee had been previously paid.

securities, or any combination thereof. Cal Water requests that the financing authority be effective until December 31, 2010.

Issuance of Equity Securities

Cal Water proposes to issue equity in the form of shares of (a) its common stock and/or (b) preferred stock solely to its parent company, Group. Group is Cal Water's only shareholder and owns all of its outstanding common and preferred shares.

Issuance of Debt Securities

If Cal Water issues debt securities, it shall not exceed in the aggregate \$250,000,000 when combined with the equity financing referenced. Because of the possibility of changing market conditions over the period covered by the Application, Cal Water desires to retain the maximum degree of flexibility for its decisions as to the timing, size and terms of the debt offering(s). Debt issues may include one or more types of financial obligations: First Mortgage Bonds or Senior Notes.

Debt securities will be issued in substantially the same form and with terms and conditions similar to Cal Water's outstanding indebtedness. As of December 31, 2003, Cal Water has two types of debt securities outstanding. First Mortgage Bonds are secured debt securities with specific assets designated as security at the time of issuance. First Mortgage Bonds have a higher standing than the unsecured debt. This debt generally has sinking fund payments. The First Mortgage Bonds are managed through a third party Trustee to oversee the security interest provisions. If a designated security asset is sold or disposed of, a replacement asset of equal or greater value must be submitted to the Trustee and a filing is made to record a security interest. The First

Mortgage Bonds have premiums for early retirement. Interest payments are semi-annual.

Senior Notes are unsecured debt and have a lower standing than the First Mortgage Bonds, but a higher standing than general creditors. Except Notes G and H, the Senior Notes do not have sinking fund payments, and the entire principal is due at maturity. All Senior Notes are of equal ranking in the event of a default. Interest payments are semi-annual. Cal Water manages the Senior Notes.

Cal Water anticipates that the debt securities will be sold for cash at 100% of par value, plus accrued interest from the date of issuance, and an interest rate to be determined by Cal Water's Board of Directors, or a Committee thereof, in light of market conditions at the time of sale. Cal Water anticipates that debt securities would range in maturity from five years to thirty years, and would be redeemable at the option of Cal Water at any time prior to maturity, subject to certain restrictions. Redemption restrictions may state a redemption price ranging from an amount equal to the principal amount plus a premium, expressed as a percentage of the principal amount, commencing with the 12-month period beginning with the date of the debt issuance or under some other type of "make-whole" formula³ or utilizing a combination of both methods, plus, in each case, accrued interest.

³ The excess amount of the discounted value of the remaining scheduled payments for the principal called for redemption over the amount of such called principal. The Make-Whole Amount may in no event be less than zero. For purposes of the discounted value, the rate is equal to the interpolated yield of a U.S. Treasury security with maturity equal to the remaining life of the called bonds plus 50 basis points.

In order to issue Mortgage debt securities, Cal Water would be required under its First Mortgage Indenture to issue each series of new Mortgage debt securities with a supplemental indenture to be executed and delivered by Cal Water. Such supplemental indenture would set forth, among other things, the aggregate principal amount, interest rate, redemption and sinking fund requirements, and the maturity date of that series of the Mortgage debt securities. Cal Water requests authorization to execute and deliver, as necessary, a First Mortgage Indenture, and each supplemental indenture in the form which Cal Water believes appropriate and which reflects the terms of the Mortgage debt securities.

Cal Water has undertaken to refinance its outstanding debt obligations to lower costs of capital for its customers. Due to the recent favorable market conditions, Cal Water refinanced approximately \$100,000,000 of existing debt from the proceeds of debt securities issued under the authority granted by D.02-03-017 dated March 6, 2002 in A.02-01-002. This refinancing reduced the annual interest costs of its customers by \$2,000,000. Cal Water's intended use of proceeds as shown in A.02-01-002 included the retirement of maturing long-term debt and for other purposes allowed under Pub. Util. Code § 817. However, at that time, Cal Water had not determined any specific amount of long-term debt to be retired or refinanced, and accordingly, no amount intended for such use was stated in A.02-01-022 and no credit was claimed. Cal Water paid in full the \$131,000 fee prescribed by Pub. Util. Code § 1904(b) for the \$250,000,000 authority requested in A.02-01-002. Because Cal Water actually did a refinancing of its existing debt from the new money issued through D.02-03-017, it now claims credit for the refinancing amount thus

used, when the Pub. Util. Code § 1904(b) fee is assessed for the financing authority requested in this Application.

Cal Water's request for credit in this Application raises no questions that should dissuade us from giving favorable consideration to the fee exemption requested. Moreover, the request is consistent with the provision in Pub. Util. Code § 1904(b) to the effect that a fee need not be paid on the portion of a debt issue that is used to refund debt on which a fee had previously been paid to the Commission. For this Application, we will grant the requested fee exemption.

The fee for this financing authority as set forth by Pub. Util. Code § 1904(b) is \$81,000.⁴

Use of Proceeds

Cal Water proposes to use the proceeds from the sale of New Securities, after payment and discharge of obligations incurred for expenses incident to their issuance and sale, to discharge all or a portion of Cal Water's then existing short-term debt obligations and to the extent there are proceeds remaining, to provide for the acquisition of property or for the construction, completion, extension or improvement of Cal Water's facilities, refunding of existing long-term debt obligations, and projected cash requirements during the next five calendar years.

Pub. Util. Code § 817(b) allows a public to issue stocks or evidences of indebtedness payable at a period of more than 12 months for the construction, completion, extension, or improvement of its facilities. Also, Pub. Util. Code § 817(d) allows a public utility to issue stock or evidences

⁴ The amount subject to the fee is \$150,000,000 (\$250,000,000 debt or equity securities less \$100,000,000 exemption for which fees have previously been paid). The fee is determined as follows: $(\$2 \times (1,000,000/1,000)) + (\$1 \times (9,000,000/1,000)) + (\$0.50 \times (140,000,000/1,000)) = \$81,000$.

of indebtedness payable at a period of more than 12 months for the discharge or lawful refunding of its obligations.

Pub. Util. Code § 818 requires an order authorizing the issue of bonds, notes, or other evidences of indebtedness payable at periods of more than 12 months.

Pub. Util. Code § 823(d) provides that no note payable at a period of not more than 12 months after the date of issuance of such note shall, in whole or in part, be refunded by any issue of stocks or stock certificates or other evidence of interest or ownership, or of bonds, notes of any term or character, or any other evidence of indebtedness, without the consent of the Commission.

The acquisition of water systems should be done by separate filing and subject to Commission approval. As stated in Resolution W-4462 dated April 22, 2004, in Cal Water's acquisition of water companies, (1) General Order (G.O.) 96-A, D.97-03-028 and Pub. Util. Code § 702 require utilities to obtain Commission approval to expand service territory, and (2) Pub. Util. Code §§ 451 and 454 require utilities to obtain Commission approval to charge rates for water service prior to the commencement of said service. Utilities will be in violation of Commission decisions and provisions of the Pub. Util. Code if they fail to seek Commission approval to expand its service territories, acquire other utilities, and collect rates not authorized by this Commission.

Further, Pub. Util. Code § 851 requires Commission authorization before a utility may "merge, acquire, or control...any public utility organized and doing business in this state...." The purpose of this and related sections is to enable the Commission, before any transfer of public

utility property is consummated, to review the situation and to take such action, as a condition of the transfer, as the public interest may require.

To the extent that any part of the proceeds from the issue of debt or equity securities authorized herein could be used to purchase water systems, expansion of service territory, or for improvements that would be subject to inclusion in ratebase for rate of return (ROR) calculation, Cal Water must disclose in any request for ROR treatment of said acquisition, expansion, or improvement, the source of funding and repayment method. Cal Water should include in a rate case filing, the decision number granting the authority to issue debt, if the proceeds of which are used for the acquisition, expansion, or improvement of facilities.

Cal Water's proposed use of proceeds is for proper purposes and is not adverse to the public interest. For purposes of this Application and pursuant to Pub. Util. Code § 818 and 823(d), we will approve Cal Water's intended use of proceeds (including retirement and discharge of short-term debt) from the proposed issue of equity and debt securities.

We remind Cal Water to obtain regulatory authorizations for all mergers or acquisitions, and impositions of charges or rates related thereto, as discussed above.

Pursuant to Pub. Util. Code § 851, we will allow Cal Water to encumber its property whenever such encumbrance serves to secure the debt authorized herein.

We place Cal Water on notice that the reasonableness of any resulting interest rate and cost of money arising from debt capital is normally subject to review in cost of capital or general rate case proceedings.

Competitive Bidding Rule

The Competitive Bidding Rule set forth in Resolution (Res.) F-616 dated October 1, 1968, exempts bond issues of \$20,000,000 or less from the competitive bidding requirement. Cal Water indicates in the Application that it will limit its debt offering of Senior Notes and First Mortgage Bonds to \$20,000,000 or less per issuance and/or no one purchaser will be permitted to acquire more than \$20,000,000 of debt securities in a calendar year.

Under the provisions of Res. F-616, Cal Water's proposed debt securities may be exempted from the Commission's Competitive Bidding Rule because no one series will exceed \$20,000,000 and/or no one purchaser will be permitted to acquire more than \$20,000,000 in a calendar year.

We grant Cal Water's request for exemption from the Competitive Bidding Rule for the previously described debt issue. Nevertheless, in the event that Cal Water finds it necessary to go beyond the \$20,000,000 threshold, such public offerings of notes or bonds in the principal amount of over \$20 million to \$200 million must comply with Res. F-616.

Financial Information

For the period ending December 31, 2003, Cal Water reported total operating revenues of \$261,070,980 (excluding Non-Regulated operations) and net income of \$13,700,777, as shown in its Pro Forma Income Statement and Return on Equity, attached as Exhibit B to the Application.

A.04-03-033 WATER/ICRJ/RHG DRAFT

Cal Water's Balance Sheet at December 31, 2003, Exhibit A to the Application, is summarized as follows:

<u>Assets</u>	<u>Amount</u>
Net Utility Plant	\$720,000,714
Investment in Non-Utility Property	2,706,127
Current Assets	40,287,008
Other Assets	<u>74,839,194</u>
Total Assets	<u>\$837,833,043</u>
<u>Capitalization and Liabilities</u>	
Common Stockholders' Equity	\$231,715,640
Preferred Stock	<u>3,475,000</u>
Total Equity	\$235,190,640
Long Term Debt	\$269,720,790
Current Liabilities	59,404,353
Unamortized Investment Tax Credit	2,924,616
Deferred Income Taxes	37,629,717
Regulatory and Other Liabilities	35,597,797
Advances for Construction	121,049,045
Contributions in Aid of Construction (CIAC)	<u>76,316,085</u>
Total Liabilities	\$602,642,403
Total Capitalization and Liabilities	<u>\$837,833,043</u>

Construction Budget

Cal Water's Projected Company Funded Expenditures for Utility Plant for 2004 through 2009, as shown in Exhibit D to the Application, are as follows:

<u>Components</u>	(dollars in thousands)						<u>Total</u>
	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	
Land & Land Rights	1,194	1,004	1,200	1,250	1,300	1,307	7,255
Structures & Improvements	3,468	7,251	3,200	3,300	3,400	3,417	24,036
Wells	2,948	2,539	7,050	7,500	7,600	7,638	35,275
Storage	5,182	8,657	5,050	5,100	5,200	5,226	34,415
Pumping & Water Treatment Equipment	9,081	19,996	19,500	20,000	20,500	20,603	109,680
Transmission & Distribution Mains	24,545	29,252	19,250	19,500	19,800	19,899	132,246
Services	3,277	3,253	3,500	3,600	3,800	3,819	21,249
Meters	3,001	3,059	3,100	3,200	3,300	3,317	18,977
Hydrants	712	720	800	850	900	905	4,887
General Equipments	<u>7,001</u>	<u>7,181</u>	<u>7,350</u>	<u>7,500</u>	<u>7,700</u>	<u>7,739</u>	<u>44,471</u>
Construction Total	<u>60,409</u>	<u>82,912</u>	<u>70,000</u>	<u>71,800</u>	<u>73,500</u>	<u>73,870</u>	<u>432,491</u>

We will not make a finding in this decision on the reasonableness of Cal Water's projected construction program. Construction expenditures and the resulting plant balances in rate base are issues that are normally addressed in general rate cases.

Projected Cash Requirements

Cal Water's estimate of cash requirements for 2004 through 2009 is summarized as follows:

<u>Components</u>	(dollars in thousands)						<u>Total</u>
	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	
Construction Budget	60,409	82,912	70,000	71,800	73,500	73,870	432,491
Tax on CIAC	1,100	1,500	1,900	2,300	2,700	3,100	12,600
Extension Refunds ⁵	4,728	4,492	4,221	4,221	4,058	4,212	25,932
Maturity of Bonds	470	467	453	466	318	325	2,499
Short-Term Debt							
Payments, Net	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total Cash Requirements	66,707	89,371	76,574	78,787	80,576	81,507	473,522
Less: Cash Received from							
Internal Sources	<u>27,108</u>	<u>33,300</u>	<u>34,493</u>	<u>36,472</u>	<u>42,139</u>	<u>48,516</u>	<u>222,028</u>
External Financing	39,599	56,071	42,081	42,315	38,437	32,991	251,494
% of Available Cash							
to Needed Funds	41%	37%	45%	46%	52%	60%	

Cal Water's projected cash requirements indicates that internally generated funds will provide approximately \$222,028,000 or 47% of its total cash requirements of \$473,522,000 for years 2004 through 2009. The requested \$250 million equity and debt financing is necessary to help Cal Water meet its \$251,494,000 external funds requirements.

⁵ Pertains to CIAC Main Extension Contracts.

Capital Ratios

Cal Water's capital ratios as of December 31, 2003, are presented below as recorded and adjusted to give pro forma effect to a projected issuance of \$125,000,000 Common Stock and \$125,000,000 of debt securities requested in the Application:

	(dollars in thousands)				
	<u>Recorded</u>		<u>Adjustments</u>	<u>Proforma</u>	
Common Stock Equity	231,716	45.9%	125,000	356,716	47.2%
Preferred Stock	<u>3,475</u>	<u>0.7%</u>	<u>-</u>	<u>3,475</u>	<u>0.5%</u>
Total Equity	235,191	46.6%	125,000	360,191	47.7%
First Mortgage Bonds	26,900	5.3%	-	26,900	3.6%
Senior Notes	240,000	47.5%	125,000	365,000	48.3%
Other Long Term Debt	<u>2,821</u>	<u>0.6%</u>	<u>-</u>	<u>2,821</u>	<u>0.4%</u>
Sub-Total	269,721	53.4%	125,000	394,721	52.3%
Total Capitalization	<u>504,912</u>	<u>100.0%</u>	<u>250,000</u>	<u>754,912</u>	<u>100.0%</u>

Capital structures are normally subject to review in cost of capital or general rate case proceedings. We will not, therefore, make a finding in this decision of the reasonableness of the projected capital ratios for ratemaking purposes.

In Resolution (Res.) ALJ 176-3132 dated April 22, 2004, the Commission preliminarily categorized this Application as ratesetting, and preliminarily determined that hearings were not necessary. No protests have been received. Given these developments, a public hearing is not necessary, and there is no need to alter the preliminary determinations made in Res. ALJ 176-3132.

Comments on Draft Decision

This is an uncontested matter in which the decision grants the relief requested. Accordingly, pursuant to Pub. Util. Code 311(g)(2), the otherwise applicable 30-day period for public review and comment is being waived.

Assignment of Proceeding

Izetta C.R. Jackson is the assigned Examiner in this proceeding.

Findings of Fact

1. Cal Water, a California corporation, is a water utility subject to the jurisdiction of this Commission.
2. Cal Water needs external funds for the purposes set forth in the Application.
3. The money, property, or labor to be procured or paid for by the proposed debt issue is reasonably required for the purposes specified in the Application.
4. Authorizing Cal Water to offer, issue and deliver debt securities with interest rates based on existing market conditions at the time of negotiating the terms, as set forth in the Application is not adverse to the public interest.
5. Authorizing Cal Water to encumber utility assets in the event that such encumbrance will be required to secure the debt issue is for proper purposes and is not adverse to the public interest.
6. Cal Water refinanced \$100,000,000 of its debt from the issue of debt securities authorized by D.02-03-017.
7. Since Cal Water did not project any refinancing of existing debts in D.02-03-017, the utility paid the full fee required by Pub. Util. Code § 1904(b) for the debt authority granted in that proceeding.

8. Granting Cal Water credit for its recent \$100,000,000 refinancing of debt securities from the Pub. Util. Code § 1904(b) fee to be assessed in this proceeding is for proper purposes and is not adverse to the public interest.

9. The reasonableness of any resulting interest rate and cost of money arising from debt capital are normally subject to review in cost of capital or general rate case proceedings.

10. The Commission does not by this decision determine that Cal Water's construction budget, cash requirements forecast, and capital ratios presented herein are necessary or reasonable for ratemaking purposes. These issues are normally tested in general rate case or cost of capital proceedings.

11. Notice of the filing of the Application appeared on the Commission's Daily Calendar of April 1, 2004. There is no known opposition to this Application, and the authority requested should be granted.

Conclusions of Law

1. A public hearing is not necessary.
2. The Application should be granted to the extent set forth in the order that follows.
3. This authorization is not a finding of the value of Cal Water's stock or property, nor does it indicate approval of matters subject to review in ratemaking proceedings.
4. Res. No. F-616 specifically exempts debt issues of \$20,000,000 or less from the Competitive Bidding Rule.

5. Pub. Util. Code § 818 requires Commission authorization for the issue of stocks, bonds, notes, or other evidences of indebtedness payable at periods of more than 12 months.

6. Pub. Util. Code § 851 requires Commission authorization before a utility could merge, acquire, or control any public utility.

7. G.O. 96-A, D.97-03-028 and Pub. Util. Code § 702 require utilities to obtain Commission approval to expand service territory.

8. Pub. Util. Code §§ 451 and 454 require utilities to obtain Commission approval to charge rates for water service prior to the commencement of said service.

9. Cal Water should be exempt from the Competitive Bidding Rule because it will not issue any one series of debt securities in excess of \$20,000,000 and will not sell more than \$20,000,000 in total during any calendar year to any one purchaser.

10. Pub. Util. Code 1904(b) provides that no fee need be paid on such portion of any such issue as may be used to guarantee, take over, refund, discharge, or retire any stock, bond, note or other evidence of indebtedness on which a fee has already been paid to the Commission.

11. Cal Water should pay the fee for the authority granted in this order as determined in accordance with Pub. Util. Code § 1904(b).

12. The following order should be effective on the date of signature.

ORDER

IT IS ORDERED that:

1. California Water Service Company (Cal Water), on or after the effective date of this order and on or before December 31, 2010, upon terms and conditions substantially consistent with those set forth or contemplated in Application 04-03-033 (Application), is authorized to:

- a) Issue, sell, and deliver New Securities not exceeding \$250,000,000 in aggregate principal offering amount, said securities consisting of common shares, preferred shares or debt securities, including First Mortgage Bonds and Senior Notes;
- b) Execute and deliver any and all related documents required for the completion of the proposed financing, including, without limitation, an indenture or supplemental indenture; and
- c) Encumber its assets in connection with the debt issue.

2. Cal Water shall apply the proceeds of the New Securities authorized for the purposes specified in their Application and discussed in this Decision.

3. Cal Water shall disclose in its rate case filing if the funds used for the acquisition of water systems, expansion of service territory, or improvements are derived from the proceeds of the debt or equity securities authorized by this Decision.

4. Cal Water shall file by the application process for any acquisition of water system and related imposition of charges or rates.

5. Cal Water shall file with the Audit and Compliance Branch of the Water Division, copies of the agreements and indenture within thirty days of the execution of these documents.

6. Cal Water's proposed issuance and sale of debt securities as specified in the Application and discussed in this Decision is exempted from the requirements of the Commission's Competitive Bidding Rule. All other issues of debt securities, other than tax-exempt securities, over \$20 million but not greater than \$200 million, are subject to the Competitive Bidding Rule.

7. On or before the 25th day of each month, Cal Water shall file the reports required by General Order Series 24 with the Audit and Compliance Branch of the Water Division. Cal Water shall include in this report if any proceeds from the \$250,000,000 amount of debt and equity capital authorized herein, have be used for retirement or refunding of long-term debt securities previously issued.

8. The authority granted by this order shall become effective when Cal Water pays \$81,000 as required by Public Utilities Code § 1904(b).

9. The Application is granted as set forth above.

10. Application 04-03-033 is closed.

This order is effective today.

Dated _____, at San Francisco, California.